Buying Time
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THE FEDERAL DIARY

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By Mike Causey
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Federal, state and local government workers interested in retiring to beat a proposed change in pension tax rules would have until July 1 under the tax reform bill approved tentatively Friday by the House Ways and Means Committee.

The committee's change of heart, moving the effective date of the new pension tax from January to July, is good news for retirement-age feds who thought they had to pull the plug this year to stay under the current, more generous pension tax system.

It also increases the likelihood that the date may be further extended—to benefit senior members of Congress serving their last term—as the massive and complex reform bill works its way through Congress.

If approved, the pension tax change would wipe out the tax-free period for retirement income. Committee sources estimate that it would bring in an additional $2.5 billion in tax revenues.

Currently pensions of retirees who have contributed to their retirement funds—most of them former state and federal workers—aren't taxed until the retirees have recovered all their contributions, because they have already paid taxes on those contributions. The tax-free period can run for three years. For the typical civil service retiree, it lasts about 18 months.

The tax reform bill would subject part of the pension to immediate taxes, prorated on the estimated remaining life of the retiree. It would not be expected to increase the total taxes paid in retirement, but would eliminate the tax-free post-retirement period.

The Federal Government Service Task Force says that the typical federal retiree would pay about $10,000 in taxes in the first three years of retirement.

Most federal workers take the tax-free period into consideration when making retirement plans. Many take other jobs for that period, or cash in stocks or investments that can be taxed at lower rates when pensions aren't being counted as income.

Critics say the sudden elimination of the tax-free period would create financial problems for new retirees, and could force thousands of employes to retire before the deadline. That is the primary reason the committee extended the deadline until next summer.

Federal workers who are watching the tax reform bill should be aware that this is not the last chapter. The bill must still clear the House, then go through the Senate. The final version could be very different, and effective dates could be changed again and again.

For now, however, the pressure to retire is off because of the new July deadline.

Some insiders anticipate a further extension once longtime members of Congress who are planning to retire in January 1987 realize what the tax change would mean to them. House Speaker Thomas P. O'Neill Jr. (D-Mass.) is one of that group.

Because members of Congress have bigger salaries—and make bigger pension contributions—they have more to gain from the tax-free period than the typical civil servant. And they have much more to lose financially if they are caught on the wrong side of the deadline.